

## US inflation confirms the Fed has much more work to do

US inflation is above 9%, but it is the breadth of the price pressures that is really concerning for the Federal Reserve. With supply conditions showing little sign of improvement the onus is on the Fed to hit the brakes via higher rates to allow demand to better match supply conditions. The recession threat is rising



**9.1%** Fastest US inflation rate since November 1981

### Well at least it isn't 10%

June US inflation came in at 1.3%MoM/9.1% YoY for headline and 0.7%MoM/5.9% for core. Both

readings are 0.2pp higher than the consensus was expecting and should all but confirm a 75bp hike on July 27th following the firm June jobs print. This is the fastest rate of headline inflation since November 1981 with the only crumb of comfort being that it didn't come in as high as the fake report doing the rounds yesterday suggesting a 10% headline reading.

## US annual inflation rate (YoY%)

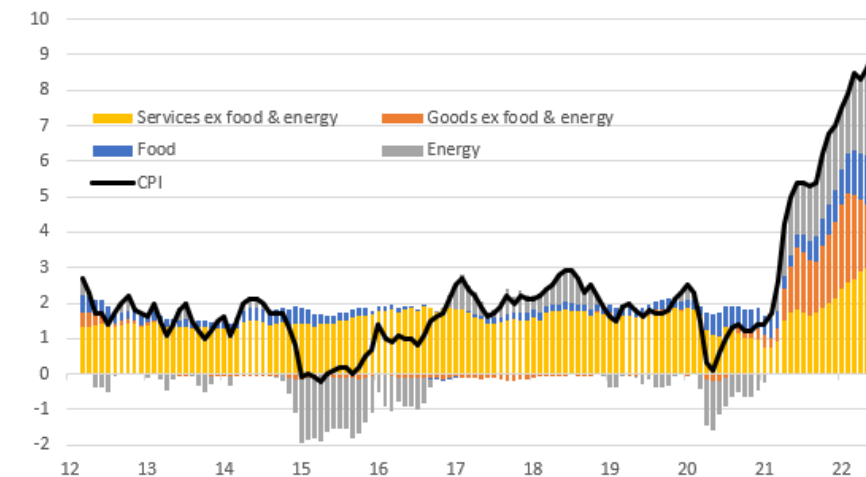


Source: Macrobond, ING

While the core rate did at least slow from 6% to 5.9%, there is not much here that will relieve the pressure on the Federal Reserve to do more to get a grip on inflation. Food prices rose another 1% month-on-month (10% year-on-year), gasoline was up 11.2% MoM (59.9% YoY) while shelter, the biggest component of CPI with a weight of 32%, is up 0.6% MoM. There were also upside surprises from apparel (+0.8% MoM) and used cars (+1.6%), which we thought might have actually dipped marginally. The only major component to see a fall was airline fares (-1.8%), but this does follow three consecutive months of double-digit monthly rises.

We are hopeful that this marks the peak for headline inflation, especially with gasoline prices down around 5% from their June peak, but we can't rule out another supply shock. In any case we suspect the descent will be slow given the ongoing upward pressure on food prices and the long time it takes for turning points in house price appreciation to feed through into the shelter components of CPI. There is still a lot of pent-up demand in the economy, especially around leisure, hospitality and tourism, as people appear prepared to run down accumulated savings and pay higher prices to do things they missed out on over the past couple of years. Hence why service sector inflation is looking so strong right now.

## US services inflation outpacing goods



Source: Macrobond, ING

## Demand is still exceeding the supply capacity of the economy

To get inflation meaningfully lower quickly we need demand to better match the supply capacity of the economy. Ideally this would come via the supply channel. Firstly, reduced geopolitical risk to get energy prices lower. Secondly, supply chains easing to improve flows of inputs and lessen pricing power and thirdly, more labour supply to fill the vacancies in the US and again take a bit more steam out of the employment cost story. But it isn't happening and may not happen for some time – hence why the Fed has thrown in the towel on the notion that inflation would be transitory.

## Fed funds to reach 3.5-3.75% by year-end

Instead, the Federal Reserve now acknowledges the onus is on them to hit the brakes on demand via higher interest rates. But by delaying their response and now having to move policy faster and deeper into restrictive territory, there is clearly the fear of a recession. The Fed has accepted that weaker growth is the price we have to pay to get inflation under control

We continue to expect 75bp hike in July with 50bp moves in September and November, followed by a 25bp hike in December taking the Fed funds range to 3.5-3.75% by year-end.

### Author

**James Knightley**

Chief International Economist

[james.knightley@ing.com](mailto:james.knightley@ing.com)

### Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial

instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.